

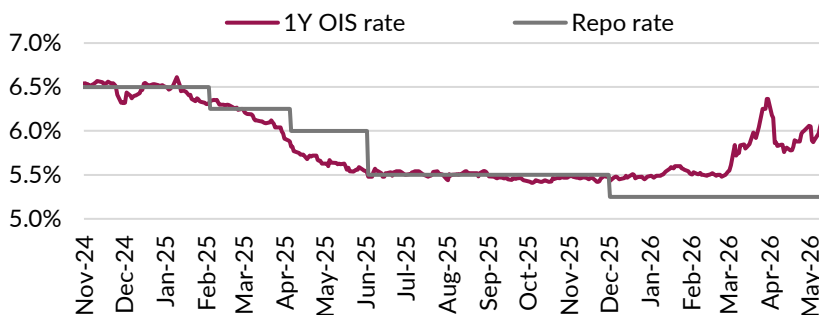
Economic Research | India

1-year OIS pricing five rate hikes. Will history repeat? It depends

Markets are now pricing in 5-6 rate hikes over the next 12 months: the 1Y OIS (average expected repo rate over the next 12 months) has climbed to 6.3%. Since 2010, this has correctly predicted all four hiking cycles, though it missed on magnitude twice. However, i) OIS began to rise on the day of the Iran conflict and may reverse if the Strait reopens; and ii) we expect several other options to be explored before rates are hiked to stabilize the INR. The step-jump in prices due to higher oil/weaker INR does not warrant monetary policy shifts; slack in the economy means inflation is not sticky. Sustained fiscal support can broaden these shocks into generalised inflation, but not immediately.

18 May 2026
Monetary Policy
Money Markets

Exhibit 1: How many rate hikes by the RBI are likely in the next 12 months?



Source: Bloomberg, Axis Bank Research

Markets expect rate hikes to start in less than six months; 5-6 hikes in a year

Overnight Index Swap rates (OIS) indicate market expectations of repo rates: e.g., the 12-month OIS is the expected average of daily repo rates over the next 12 months. Pre-war, the 12M OIS only expected the Dec-2025 rate cut to be reversed (Fig 1). But it has risen sharply since 28-Feb (start of Iran war) to 6.3%, implying 5-6 25bps hikes over the next 12 months. In the past, the 1Y OIS rate has been a reliable leading indicator of the direction of policy rates (Fig 2), though in two of four episodes the magnitude of hikes was 'overstated'.

OIS spiked with Iran war; slack in economy means sticky inflation still unlikely

OIS rates have increased globally by varying levels after the Iran war broke out (Fig 12), due to the expected inflation from supply disruptions: higher energy prices and second order effects on other goods and services. In India, INR depreciation necessitated by the terms-of-trade shock also raises risk of imported inflation. Importantly for repo rates: i) OIS rise is directly tied to the Iran conflict (not yet due to adverse weather); and ii) these are step-jumps in prices (i.e., YoY inflation would fade after a year), whereas monetary policy needs to respond to sticky inflation ([link](#)), which is low given the slack in the Indian economy. That said, sustained fiscal support can broaden these shocks into generalised inflation ([link](#)).

Will history repeat? The answer remains in the oil markets

OIS markets have had '4-in-4' predictive success since 2010, and the two episodes where hikes were lower than OIS-predicted had idiosyncratic factors: i) In the 2013-14 taper tantrum, repo was not the target rate, and WACR did peak close to 1Y OIS; ii) In 2018 hikes were despite low inflation ([link](#)) but triggered by ~15% INR depreciation (a policy error, in our view). History, thus, suggests a high likelihood of a 50bps hike in the next 12 months. However, we expect 1Y OIS to reset lower if the Strait of Hormuz reopens and oil markets ease in the next few months. A rate hike to stabilize the INR, we believe comes very late in the list of options available to address the dollar liquidity problem stressing INR currently. Better options include raising fuel prices further and cutting taxes on FPI debt ([link](#)).

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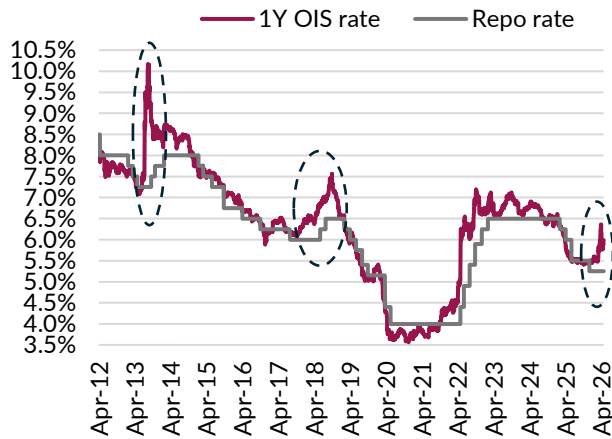
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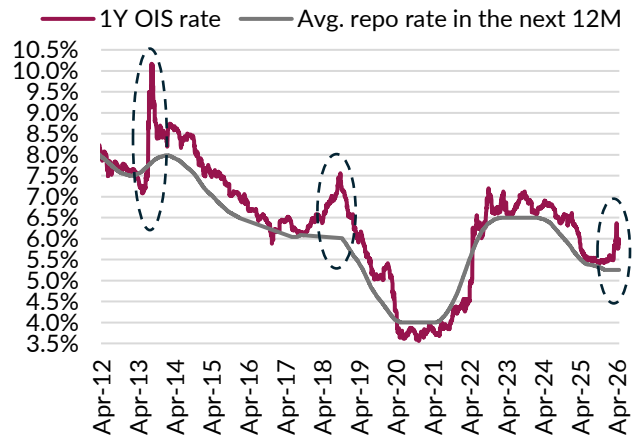
Story in Charts

Exhibit 2: 1Y OIS, unsurprisingly, has usually been a reliable leading indicator of policy rate path for 1Y horizon



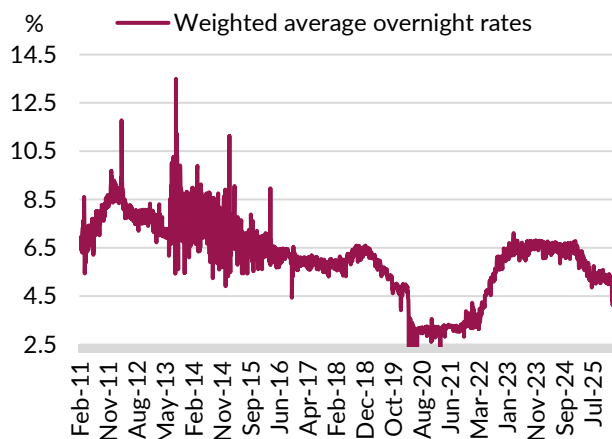
Source: Bloomberg, Axis Bank Research

Exhibit 3: The gap is mostly a small term-premia plus "distortion" which occurs during periods of systemic risk



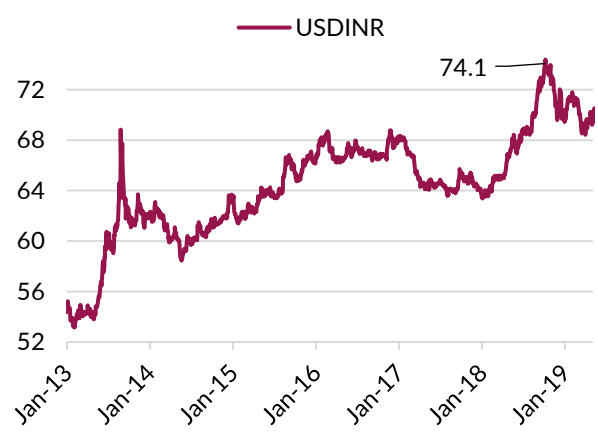
Source: Bloomberg, Axis Bank Research

Exhibit 4: 1Y OIS captured volatility in O/N rates during the taper tantrum episode (this 'explains' the first 'anomaly')



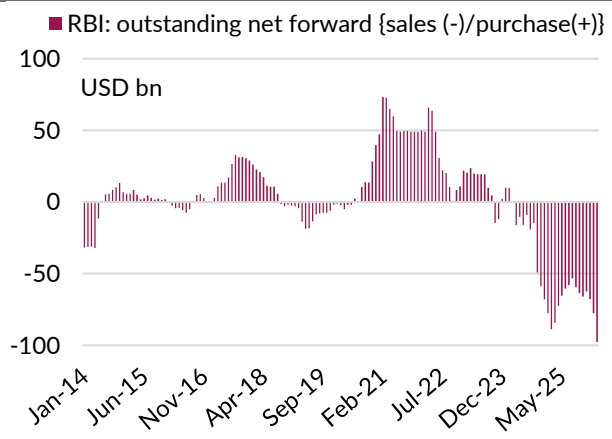
Source: RBI, Axis Bank Research

Exhibit 5: By Sep-18, 1Y OIS rate was elevated as INR had depreciated ~15%; INR appreciation erased pricing of hikes



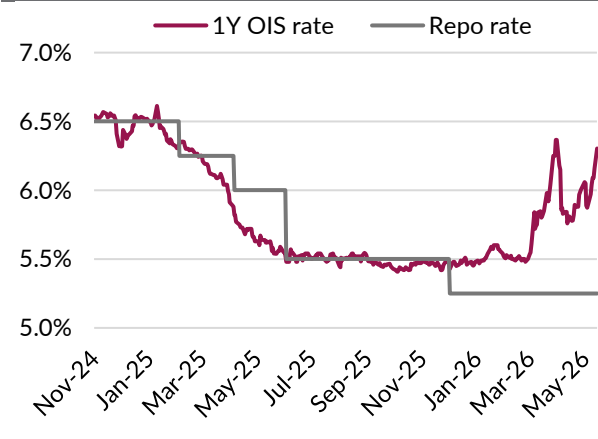
Source: RBI, Axis Bank Research

Exhibit 6: A ~10% INR appreciation (like post Oct-18) unlikely this time given the historic net short position of the RBI



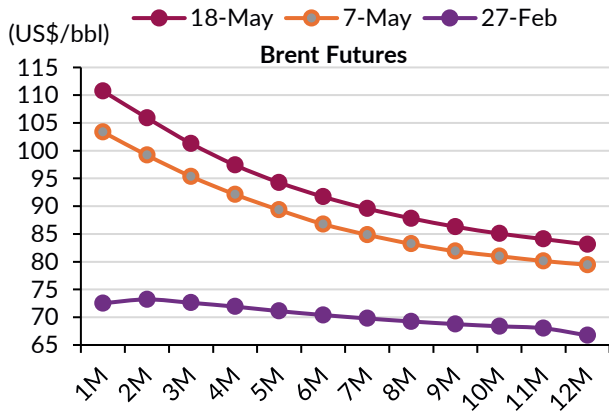
Source: Bloomberg, Axis Bank Research

Exhibit 7: 1Y OIS was steady at ~5.5% from Jun-25 to Feb-26 (despite a rate cut in Dec-25); the rate jumped only post war



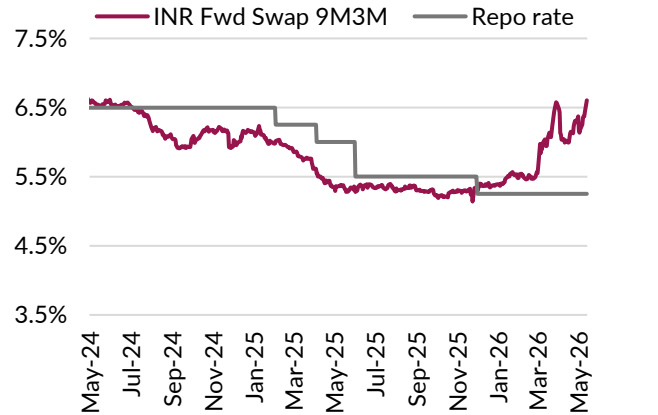
Source: Bloomberg, Axis Bank Research

Exhibit 8: Average Brent futures over next 12 months are now 33% higher vs. pre-war



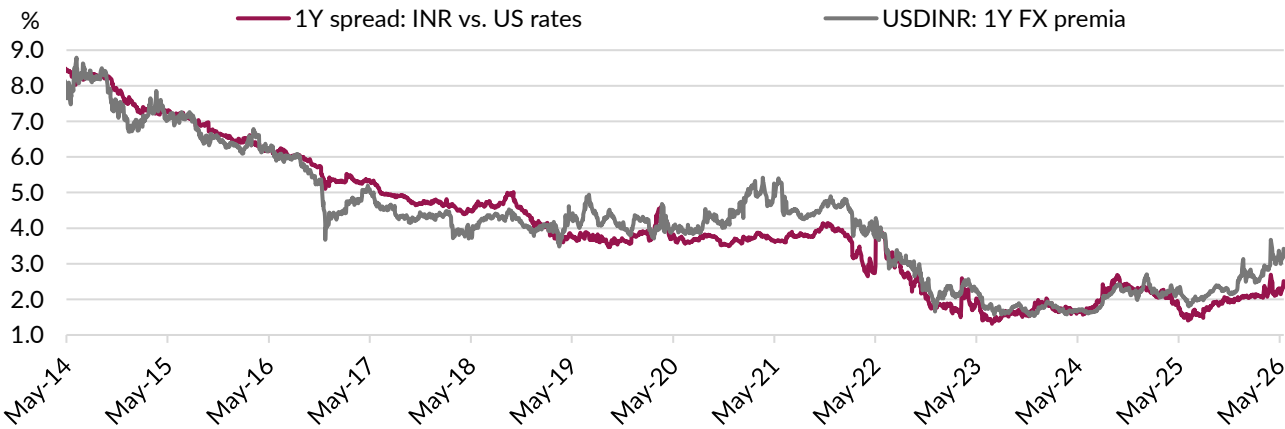
Source: Bloomberg, Axis Bank Research

Exhibit 9: 12M ahead rate expectations better measured by 9m3m swap rate vs. 1Y OIS → markets pricing 5-6 rate hikes



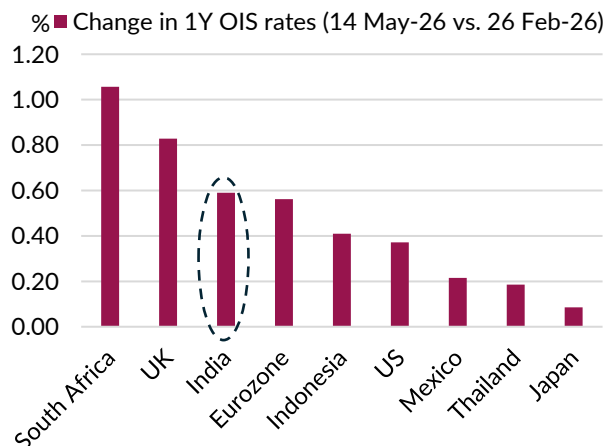
Source: Bloomberg, Axis Bank Research

Exhibit 10 -Market view: further INR depreciation and rate hikes necessary to bring 'interest rate parity' into force



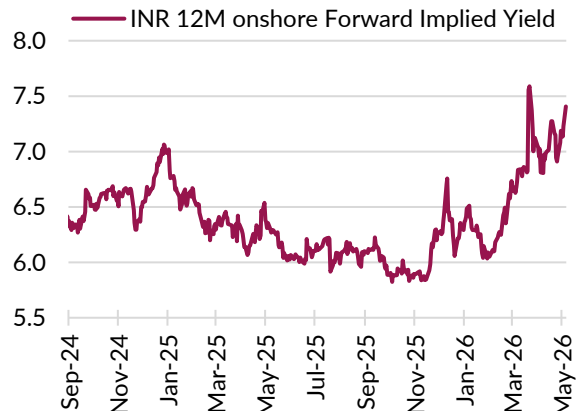
Source: Bloomberg, Axis Bank Research

Exhibit 12 -A sharp drop in USD 1Y OIS rate may lower the quantum of rate hikes priced in & INR depreciation pressures



Source: Bloomberg, Axis Bank Research

Exhibit 13 - The 12M onshore implied yield is 7.4% currently (no arbitrage condition), was ~6.2% pre-war in Feb-26



Source: Bloomberg, Axis Bank Research

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